

Internal Revenue Service

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Department of the Treasury

Washington, DC 20224

Third Party Communication: None

Date of Communication: Not Applicable

Person To Contact:

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CC:CORP:B03

PLR-124553-11

Date:

December 20, 2011

TY

Legend

Distributing =

Controlled 1 =

Controlled 2 =

Shareholder A =

Shareholder B =

Shareholder C =

Shareholder D =

State U =

Business =

V =

W =

X =

Y =

Z =

Date 1 =

Date 2 =

Dear :

We respond to your June 7, 2011 request for rulings regarding certain federal income tax consequences of a proposed transaction. The information submitted in that request, and in subsequent correspondence, is summarized below.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. This office has not verified any of the materials submitted in support of the request for rulings. Verification of the information, representations, and other data may be required as part of the audit process.

In particular, this office has not reviewed any information pertaining to, and has made no determination regarding, whether the Proposed Transaction: (i) satisfies the business purpose requirements of § 1.355-2(b) of the Income Tax Regulations; (ii) is used principally as a device for the distribution of the earnings and profits of the distributing corporation or the controlled corporations or both (see section 355(a)(1)(B) of the Internal Revenue Code (the "Code") and § 1.355-2(d)); or (iii) is part of a plan (or series of related transactions) pursuant to which one or more persons will acquire directly or indirectly stock representing a fifty percent or greater interest in the distributing corporation or the controlled corporations (see § 355(e) and § 1.355-7).

Summary of Facts

Distributing is a closely-held State U corporation that was organized as a subchapter C corporation on Date 1. Distributing elected to be treated as subchapter S corporation for federal income tax purposes more than 10 years ago on Date 2.

Distributing has V shares common stock outstanding. Shareholder A owns W shares of Distributing stock. Shareholder B owns X shares of Distributing stock. Shareholder C owns Y shares of Distributing stock. Shareholder D owns Z shares of Distributing stock. Distributing is engaged in the Business.

To resolve shareholder conflict, Distributing has proposed the following transaction (the Proposed Transaction).

Proposed Transaction

1. Controlled 1 and Controlled 2 will be formed as State U corporations. Controlled 2 will make an election under section 1362(a) to be treated as a subchapter S corporation (within the meaning of section 1361(a)). Controlled 1 and Controlled 2 will have one class of common stock outstanding, all of which will be owned directly by Distributing.
2. Distributing will transfer all of the Business assets to Controlled 1 and Controlled 2 in exchange for all of the stock of Controlled 1 and Controlled 2 and the assumption by Controlled 1 and Controlled 2 of the liabilities associated with those assets (the Contributions).
3. Distributing will distribute all of the stock of Controlled 1 to Shareholders A and B in exchange for all their Distributing stock. Distributing will distribute all of the stock of Controlled 2 to Shareholders C and D in exchange for all their Distributing stock (the Distributions). Distributing will be liquidated as part of the reorganization.

Representations

The following representations have been made with respect to the Proposed Transaction:

- a) The fair market value of the of Controlled 1 and Controlled 2 and other consideration to be received by each shareholder of Distributing will be approximately equal to the fair market value of the Distributing stock surrendered by the shareholder in the exchange.
- b) No part of the consideration to be distributed by Distributing will be received by a shareholder as a creditor, employee or in any capacity other than that of a Distributing shareholder.
- c) The five years of financial information submitted on behalf of Distributing is representative of the corporation's present operation, and with regard to such corporation, there have been no substantial operational changes since the date of the last financial statements submitted.
- d) Distributing has continuously conducted an active business, within the meaning of §1.355-3(b), for the five year period ending on the date of the Distributions.
- e) Following the Proposed Transaction, Controlled 1 and Controlled 2 will each continue independently and with its separate employees, the active conduct of its share of all the integrated activities of the Business conducted by Distributing

prior to the consummation of the Proposed Transaction. Distributing will be liquidated as part of the reorganization.

- f) No part of the Business will have been acquired during the five-year period ending on the date of the Distributions in a transaction in which gain or loss was recognized (or treated as recognized) in whole or in part.
- g) The distribution of stock of Controlled 1 and Controlled 2 is carried out for the following business purpose: to resolve shareholder conflict. The distribution of the stock of Controlled 1 and Controlled 2 is motivated, in whole or substantial part, by this corporate business purpose.
- h) The Proposed Transaction is not used principally as a device for the distribution of earnings and profits of Distributing or Controlled 1 or Controlled 2.
- i) Payments made in connection with all continuing transactions, if any, between Distributing and Controlled 1 and Controlled 2, will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.
- j) No intercorporate debt will exist between Distributing and Controlled 1 or Controlled 2 at the time of, or subsequent to, the distribution of the Controlled 1 or Controlled 2 stock.
- k) The liabilities assumed in the Proposed Transaction and the liabilities to which the transferred assets are subject were incurred in the ordinary course of business and are associated with the assets being transferred.
- l) The total adjusted bases of the assets transferred to each of Controlled 1 and Controlled 2 by Distributing will equal or exceed the sum of the liabilities assumed (within the meaning of section 357(d)), if any, by each of the controlled corporations respectively.
- m) The total fair market value of the assets that Distributing will transfer to each of Controlled 1 and Controlled 2 will exceed the sum of: (a) the amount of any liabilities assumed (within the meaning of section 357(d)) by each controlled corporation in connection with the exchange; (b) the amount of liabilities owed to each controlled corporation by Distributing (if any) that are discharged or extinguished in connection with the exchange; and (c) the amount of any cash and the fair market value of any property (other than stock and securities permitted to be received under section 361(a) without the recognition of gain) received by Distributing from each controlled corporation (if any) in connection with the exchange. The fair market value of the assets of each controlled corporation will exceed the amount of its liabilities immediately after the exchange.
- n) The aggregate fair market value of the assets contributed to each of Controlled 1 and Controlled 2 will exceed the aggregate adjusted basis of such assets immediately after the contribution.
- o) Distributing neither accumulated its receivables nor made extraordinary payment of its payables in anticipation of the transaction.
- p) No two parties to the transaction are investment companies as defined in section 368(a)(2)(F)(iii) and (iv).

- q) The Distributions are not part of a plan or series of related transactions (within the meaning of §1.355-7) pursuant to which one or more persons will acquire, directly or indirectly, stock representing 50-percent or greater interest (within the meaning of section 355(d)(4)) in Distributing and Controlled 1 or Controlled 2 (including any predecessor or successor of any such corporation).
- r) For purposes of section 355(d), immediately after the Distributions, no person (determined by applying section 355(d)(7)) will hold stock possessing 50 percent or more of the total combined voting power of all classes of Distributing stock entitled to vote, or 50 percent or more of the total value of all classes of Distributing stock, that was acquired by purchase (as defined in section 355(d)(5) and (8)) during the five year period (determined after applying section 355(d)(6)) ending on the date of the Distributions.
- s) For purposes of section 355(d), immediately after the Distributions, no person (determined after applying section 355(d)(7)) will hold stock possessing 50 percent or more of the total combined voting power of all classes of Controlled 1 or Controlled 2 stock entitled to vote, or 50 percent or more of the total value of shares of all classes of Controlled 1 or Controlled 2 stock, that was either (i) acquired by purchase (as defined in section 355(d)(5) and (8)) during the five year period (determined after applying section 355(d)(6)) ending on the date of the Distributions or (ii) attributable to distributions on distributing stock that were acquired by purchase (as defined by sections 355(d)(5) and (8)) during the five year period (determined after applying section 355(d)(6)) ending on the date of the Distributions.
- t) Immediately after the transaction (as defined in section 355(g)(4)), either (1) no person will hold a 50 percent or greater interest (within the meaning of section 355(g)(3)) in Distributing or Controlled 1 or Controlled 2, (2) if any person holds 50 percent or greater interest (within the meaning of section 355(g)(3)) in any disqualified investment corporation (within in the meaning of section 355(g)(2)), such person will have held such interest in such corporation immediately before the transaction, or (3) Distributing, Controlled 1, and Controlled 2 will not be a disqualified investment corporation (within the meaning of section 355(g)(2)).

Rulings

- (1) The transfer by Distributing to Controlled 1 of part of its assets in exchange for all of the Controlled 1 stock and assumption of liabilities followed by distribution of all the Controlled 1 stock to Shareholder A and Shareholder B will constitute a reorganization within the meaning of section 368(a)(1)(D). Distributing and Controlled 1 will be “a party to a reorganization” within the meaning of section 368(b).
- (2) The transfer by Distributing to Controlled 2 of part of its assets in exchange for all of the Controlled 2 stock and assumption of liabilities followed by the distribution of all the Controlled 2 stock to Shareholder C and Shareholder D will constitute a reorganization within the meaning of section 368(a)(1)(D).

Distributing and Controlled 2 will be “a party to a reorganization” within the meaning of section 368(b).

(3) No gain or loss will be recognized by Distributing on the Contributions. Sections 357(a) and 361(a).

(4) No gain or loss will be recognized by Controlled 1 or Controlled 2 on the Contributions. Section 1032(a).

(5) Controlled 1's basis in each asset received from Distributing in the Contributions and Controlled 2's basis in each asset received from Distributing in the Contributions will equal the basis of such asset in the hands of Distributing immediately before its transfer. Section 362(b).

(6) The holding period for each asset received by Controlled 1 and Controlled 2 from Distributing in the Contributions will include the period during which such asset was held by Distributing. Section 1223(2).

(7) No gain or loss will be recognized by Distributing on the Distributions. Section 361(c)(1).

(8) No gain or loss will be recognized by (and no amount will be included in the income of) Shareholder A and Shareholder B upon receipt of Controlled 1 stock in the Distributions. Section 355(a)(1).

(9) No gain or loss will be recognized by (and no amount will be included in the income of) Shareholder C and Shareholder D upon receipt of Controlled 2 stock in the Distributions. Section 355(a)(1).

(10) The aggregate basis of the Controlled 1 stock received by Shareholder A and Shareholder B immediately after the Distributions will be the same as each shareholder's aggregate basis in the Distributing stock surrendered in the exchange therefore, allocated in the manner described in §1.358-2(a)(2). Section 358(a)(1) and (b).

(11) The aggregate basis of the Controlled 2 stock received by Shareholder C and Shareholder D immediately after the Distributions will be the same as each shareholder's aggregate basis in the Distributing stock surrendered in exchange therefore, allocated in the manner described in §1.358-2(a)(2). Section 358(a)(1) and (b).

(12) The holding period of the Controlled 1 stock received by Shareholder A and Shareholder B and the holding period of the Controlled 2 stock received by Shareholder C and Shareholder D in the Distributions will include the holding period of the Distributing stock with respect to which the Distributions will be made, provided that such Distributing stock is held as a capital asset on the date of the Distributions. Section 1223(1).

(13) Distributing's earnings and profits will be allocated between Distributing and Controlled 1 and Controlled 2 in accordance with section 312(h) and §1.312-10(a).

(14) The accumulated adjustments account of Distributing will be allocated between Distributing and Controlled 1 and Distributing and Controlled 2 in a manner similar to the manner in which the earnings and profits of Distributing will be allocated under section 312(h) in accordance with §1.1368-2(d)(3).

(15) Provided that the Distributions are undertaken immediately after the Contributions, Distributing's momentary ownership of the stock of Controlled 1 and Controlled 2, as part of the reorganization under section 362(a)(1)(D), will not cause Controlled 1 and Controlled 2 to have been an ineligible shareholder for any portion of their respective first taxable year under section 1361(b)(1)(B) and will not, in itself, render Controlled 1 and Controlled 2 ineligible to elect to be a subchapter S corporation for their respective first taxable year.

We express no opinion about the tax treatment of the Proposed Transaction under other provisions of the Code and regulations or the tax treatment of any conditions existing at the time of, or effects resulting from, the Proposed Transaction that is not specifically covered by the above rulings.

Procedural Statements

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representatives.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of the letter ruling.

Sincerely,

Mark S. Jennings
Branch Chief, Branch 1
Office of Associate Chief Counsel (Corporate)